

OFFICE OF THE
ARIZONA
STATE
TREASURER



HON. DOUG DUCEY
TREASURER

INVESTMENT
PHILOSOPHY

SAFETY
before
LIQUIDITY
before
YIELD



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Inside the Vault

The Arizona State Treasurer's Quarterly Update

Volume 11, Issue IV

Q4 2012

Endowment Distribution Formula Simplified

Through an Act of Congress in 1863 that established the Territory of Arizona and the State Enabling Act of 1910, the Federal Government granted about 10.9 million acres of land to 14 beneficiaries, Arizona public education being the largest receiving more than 90 percent of all the proceeds. Today, about 8 million acres remain in the trust for K-12 education. Every time the state sells a piece of state land, those proceeds are deposited into the State Treasurer's Office to be managed into perpetuity.

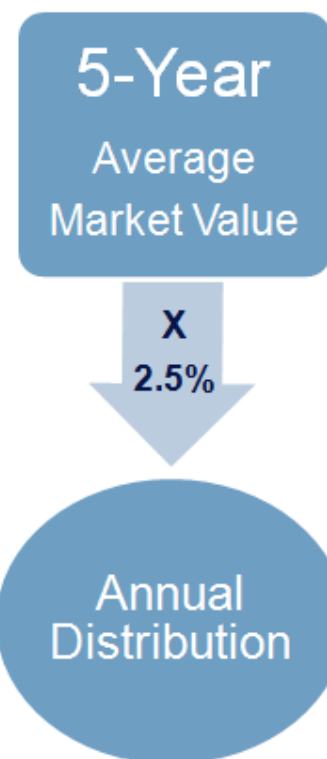
Today the market value of the Permanent Land Endowment Trust Fund is more than **\$3.6 Billion**. If that were a college endowment, it would be the twenty-first largest endowment in the country.

Article X, Section 7 of the Arizona State Constitution created the Arizona Board of Investment to serve as trustees of the Permanent Land Endowment Trust Fund. In this role as fiduciaries of the fund the Board protects Arizona's investments while maximizing returns.

Upon review of the first asset allocation study for the fund earlier this year, it became clear to the Board of Investment that the formula used to distribute earnings was critically flawed. Its complications have resulted in uneven, unpredictable and zero dollar distributions. If left unchanged, this current formula would result in several additional years, over the next decade, of zero dollar distributions.

The Board of Investment proposed a simpler distribution formula that would provide more consistency for the beneficiaries. After sharing this information with the Legislature, HCR 2056 was placed on the November ballot as Prop 118.

Prop 118 was passed by voters and now changes the Endowment distribution formula to be 2.5 percent of the average 5-year market value of the fund. With the new formula in place, K-12 education will receive **\$8.4 Million** in additional proceeds in fiscal year 2013. The distribution will revert to the old formula again July 1, 2021, barring any further action by a future Treasurer or Legislature.



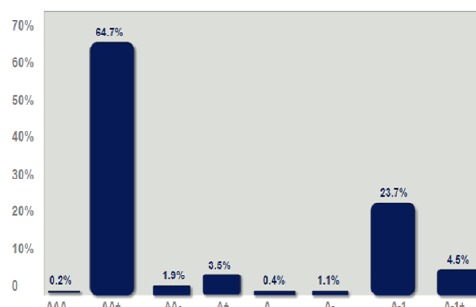
LGIP Pool 5: Short-term fund

AT A GLANCE

- \$1.12 Billion in assets with Net Asset Value at \$1.000 as of 9/30/2012.
- Diversified investments weighted to highly rated Commercial Paper first, Repurchase Agreements second and Agencies/Treasuries third.
- Focus this quarter will remain on adding commercial paper names with maturities beyond 30 days.
- Continues to maintain the highest rating of AAA/SI+.
- Weighted Average Maturity is 34 days.

Safety

Continues to receive highest rating from Standard & Poor's: AAA/SI+

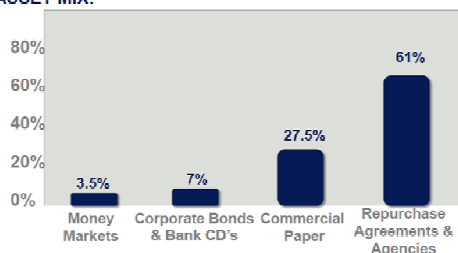


Liquidity

Weighted Average Maturity: 34 days on 9/30/2012

DURATION: 100% from 0-1 yrs

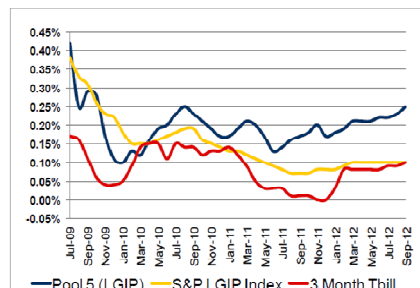
ASSET MIX:



Yield

.23% FYTD

.10% FYTD (S&P LGIP Index)

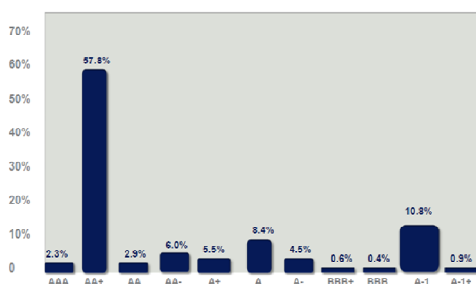


**Pool 5 YTD
Net Yield
has beaten its
benchmark by
13 basis points**

LGIP Pool 500: Medium-term fund

Safety

AA Weighted Average Rating

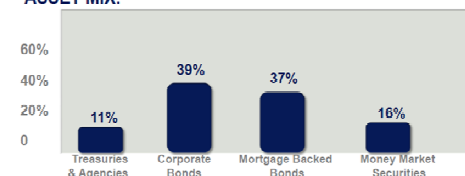


Liquidity

Effective Duration: 1.01 years on 9/30/2012

DURATION:

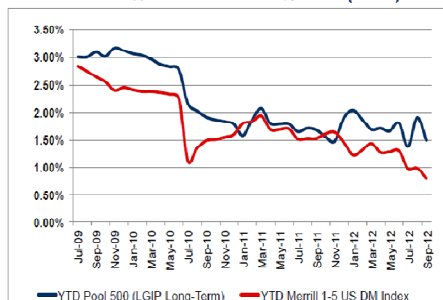
ASSET MIX:



Yield

1.60% FYTD

0.92% FYTD (Index)



**Pool 500 YTD
has beaten its
benchmark by
68 basis points**

AT A GLANCE

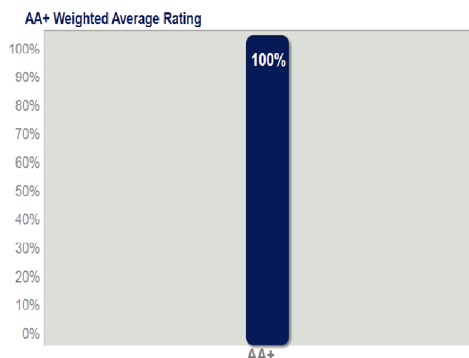
- \$268.8 Million in assets with Floating Net Asset Value at \$1.0469 as of 9/30/2012.
- Diversified fund containing Treasuries, Agencies, Corporate Bonds and Mortgages.
- The effective duration is 1.01 years.
- Keeping the fund short with 79% of the investments maturing under two years.
- Maximum exposure to any credit at 2.5%.
- Weighted Average Rating of all the securities is AA.

Pool 7 LGIP-GOV: Short-term fund

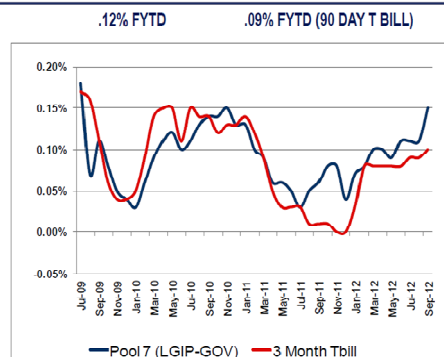
AT A GLANCE

- \$1.29 Billion Assets with Net Asset Value at \$1.00 as of 9/30/2012.
- Invested in highly liquid, low-risk securities that are backed by the full faith and credit of the U.S. Government.
- Increasing duration and laddering maturities as opportunities arise.
- For this quarter we will be looking at options to mitigate any risks of market disruptions that may arise due to the end of year fiscal cliff pressures.
- Weighted Average Maturity is 54 days.

Safety



Yield

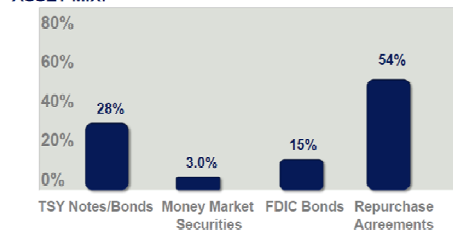


Liquidity

Weighted Average Maturity: 54 days on 9/30/2012

DURATION: 100% from 0-1 yrs

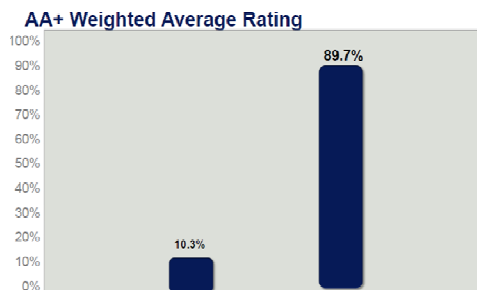
ASSET MIX:



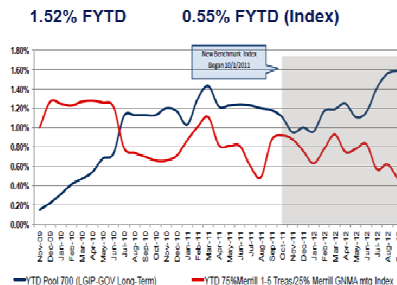
**Pool 7 YTD
Net Yield
has beaten its
benchmark by
3 basis points**

Pool 700 LGIP-GOV: Medium-term fund

Safety



Yield



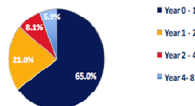
AT A GLANCE

- \$229.3 Million in assets with Floating Net Asset Value at \$1.0197 as of 9/30/2012.
- All securities are backed by the full faith and credit of U.S. Government including Treasuries, FDIC paper and GNMA Mortgages.
- The effective duration is .77 years.
- Keeping the fund short with 86% of the investments maturing in under a year.
- Weighted Average Rating of all the securities is AA+.

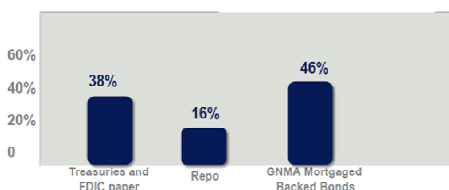
Liquidity

Effective Duration: .77 years on 9/30/2012

DURATION:



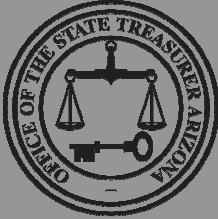
ASSET MIX:



**Pool 700 YTD
has beaten its
benchmark by
97 basis points**

OFFICE OF THE

ARIZONA STATE TREASURER



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View AZ's Daily Cash Balance at www.AZCheckbook.com

Annual Audited Financial Statements



The Treasurer's Office delivered its Fiscal Year 2012 Annual Audited Financial Statements to the Governor on October 31, 2012. Although

Arizona faced tremendous economic challenges, the Treasurer's Office continued to earn a profit for both state and local taxpayers. In Fiscal Year 2012, the office distributed investment earnings of **\$134.8 million**.

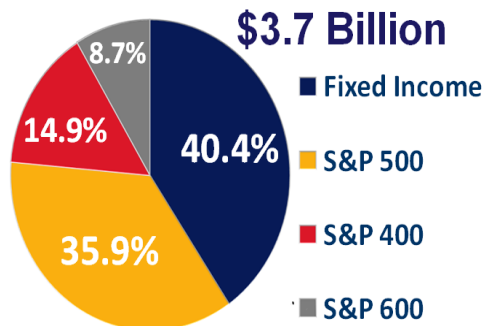
Highlights of the report include:

- Fair value of combined investments totaled **\$11.8 billion**;
- The Endowment fund totaled **\$3.5 billion**, from which **\$83.9 million** of investment earnings were distributed to the beneficiaries;
- Non-endowment funds totaled **\$8.3 billion**, from which **\$50.9 million** was distributed to pool participants;
- Custody of performance bond's cash and securities totaled **\$3.6 billion**;
- State shared revenue distributions totaled **\$9.2 billion**.

The entire report can be accessed online at www.aztreasurer.gov.

Land Endowment Asset Allocation

(as of September 30, 2012)



AZ's Savings Account (as of September 30, 2012)

\$451,085,808

Monthly Interest Earned:

July = \$201,104

August = \$439,608

September = \$382,281

AZ's Checking Account

FY 2013 Q1 Average Monthly
Cash Balance:

+70% YOY

July = \$1.816 Billion

August = \$1.474 Billion

September = \$1.419 Billion

FY 2013 Q1 Earnings \$29,673,076

